IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1960.

IRVING SACHS, Petitioner, vs. COMMISSIONER OF INTERNAL REVENUE, Respondent.	}	No. .....

PETITION FOR WRIT OF CERTIORARI

To the United States Court of Appeals
for the Eighth Circuit.

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PETITION FOR WRIT OF CERTIORARI

To the United States Court of Appeals for the Eighth Circuit.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, Irving Sachs, a resident of the County of St. Louis in the State of Missouri, respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Eighth Circuit

in the case styled "Irving Stiles, Petitioner, v. Commissioner of Internal Revenue, Respondent," affirming the judgment of the Tax Court of the United States.

The opinion of the Court of Appeals is reported at 5 A. F. T. R. 2d 1291, and a copy thereof is appended. The decision of the Tax Court of the United States is reported at 32 T. C. 815, and a copy thereof is included in the Record printed for the use of the Court of Appeals, nine copies of which are furnished pursuant to Rule 21.

JURISDICTION.

The judgment of the Court of Appeals was entered on April 20, 1960. Jurisdiction of this Court to review the judgment of the Court of Appeals is conferred by the Act of June 25, 1948, Chapter 646; 62 Stat. 928; 28 U. S. C. 1254.

QUESTION PRESENTED.

The question presented for review is whether the amounts paid by Shu-Stiles, Inc., a Missouri corporation, to discharge a fine imposed upon petitioner for acts done in his capacity as president of Shu-Stiles, Inc., constitute income taxable to petitioner under the Internal Revenue Codes of 1939 and 1954.

STATUTES INVOLVED.

The statutes involved are the Internal Revenue Code of 1939, Section 22 (a) and Section 115 (a), and the Internal Revenue Code of 1954, Sections 61 and 316. The pertinent text of the above statutes is appended.

STATEMENT OF THE CASE.

Petitioner was at all material times president and chief executive officer of Shu-Stiles, Inc., a Missouri corporation. He also owned approximately one third of the outstanding stock of that corporation, the remaining shares being owned by his brothers and one unrelated person.

On March 4, 1951, petitioner was charged by indictment with unlawfully attempting to defeat and evade income taxes owed by Shu-Stiles, Inc., for the years 1942, 1943, 1944 and 1945 by filing false and fraudulent tax returns for the corporation. Upon his plea of guilty he was fined a total of $40,000. Shortly thereafter the District Court, by appropriate order, directed the payment of the fine in installments over a period of approximately four years. Pursuant to resolution of the shareholders of Shu-Stiles, Inc., recognizing that the acts of petitioner as president of the corporation, leading up to his indictment, conviction, and assessment of the fine, were done for and on behalf of the corporation without any personal benefit to the petitioner from such acts, the corporation paid the fine in the installments permitted by the District Court, that is, during the year 1951, $5,000, plus costs of $24.50; during the year 1952, $7,500; during each of the years 1953 and 1954, $10,000; and during the year 1955, $7,500.

Petitioner did not report the amounts so paid in discharge of the fine as income for the years 1951 through 1955, and respondent asserted by notice of deficiency that the amounts so paid were taxable as income to him. Petitioner duly appealed to the Tax Court of the United States and, upon refusal of that Court to grant relief, to the United States Court of Appeals for the Eighth Circuit, which affirmed the decision of the Tax Court.

REASONS FOR ALLOWANCE OF THE WRIT.

Petitioner respectfully submits that writ of certiorari should issue, as above prayed, because the United States Court of Appeals has decided an important question of federal law which has not been but should be, settled by this Court, and has decided a federal question in a way in conflict with applicable decisions of this Court. The decision of the United States Court of Appeals is contrary to the consistent administrative practice of the respondent and contrary to the settled opinion of the informed public of the meaning of the law.

In **Tank Truck Rentals v. Commissioners**, 356 U. S. 30, this Court recently decided that the payment by an employing corporation of a fine levied upon its employee was not deductible by such corporation in computing its taxable income. This case presents the cognate question, not yet decided by this Court, whether or not the payment of such fine gives rise to the imposition of income tax upon such employee as upon the receipt of taxable income.

In stating in the case at bar that the payment of petitioner's fine was a "distribution made by a corporation to its shareholders," the Court below confuses the word "distribution," consistently used in the Internal Revenue Code, with the word "payment." Distinction between these two words is made by this Court in **Palmer v. Commissioner**, 302 U. S. 63. In holding that income exists because of reimbursement for or indemnification against loss, the Court below contradicts the meaning, definition and understanding of the word "income" set out in the Revenue Laws, enunciated by this Court and expressed in treatises by learned authors. Income is "annual or periodic wealth." It arises from a source, as the "application of labor to a capital stock." No source not within the understanding and explanation of the quoted phrase has as yet been discovered

by lawyers or economists. Income is gain or profits or income. The words, never included as part of the definition or explanation of income, "payments," "receipts," "moneys," "transfers," "circulations," represent the analysis of income made by the Court below. In holding that there can be income without economic gain, that there receipt, constructive or actual, can be income, the Court renders its decision contrary to previous decisions, texts, history and understanding.

Income is the economic gain which is the consideration for which a payment is made; and a payment for no consideration does not represent income whether or not it is denominated a gift. Yet the Court below holds that indemnification for no consideration is income, while if there is consideration it must recognize that it is not. The rule is that indemnification, even if for consideration, is not income; *a fortiori*, if for no consideration, it is not. U. S. v. Supplee-Biddle Hardware Co., 265 U. S. 18; Dobson v. Commissioner, 320 U. S. 489. The Court below holds that the payment was not for consideration, but that it was nevertheless taxable as income. A payment for no consideration is by definition a gift. The decision of the Court below is therefore contrary to **United States v. Kaiser**, decided by this Court on June 13, 1960.

This case presents the questions important in revenue legislation, of the nature of taxable income, whether income is gains, profits and income from a source, annual wealth, an economic concept, or includes all receipts and transfers. For many years this Court has not considered the general question, and, as a result, grave doubts have arisen, whether changing economic theories have changed the concepts of wealth to such an extent that income has acquired a meaning different from that ascribed to it in 1913 in the Sixteenth Amendment to the Constitution. These uncertainties result in confusion in legislation, administration and adju-

dication) in confounding income taxation with circulation taxes, making the Internal Revenue Code an incomprehensible hodge-podge. The statute recognizes that income is from a **source**, and there is no kind of income from no source. A "source" as used in the Sixteenth Amendment is an origin capable of repeating its yield indefinitely (though not necessarily eternally), as a well, a tree, a business; not a one-time grant, as a bucket of water, a basket of fruit or a donor.

Respectfully submitted,

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APPENDIX.

Opinion of Court of Appeals.

UNITED STATES COURT OF APPEALS.

For the Eighth Circuit.

No. 16,353

Irving Sachs, Petitioner, vs. Commissioner of Internal Revenue, Respondent.	Petition to Review Decision of the Tax Court of the United States.

(April 20, 1960.)

Before Vogel, Van Oosterhout, and Matthes, Circuit Judges.

Matthes, Circuit Judge.

The question is whether the amounts paid by Shu Stiles, Inc., a Missouri corporation, to discharge a fine imposed upon petitioner, who was a shareholder and the president of the corporation, constitute income taxable to petitioner under § 22 (a), § 115 (a) Internal Revenue Code, 1939, 61,

26 Internal Revenue Code, 1954. The Tax Court sustained respondent's determination that for the years 1951 through 1955 there were deficiencies in petitioner's income tax totaling $21,951.69. See 32 T. C. No. 69. It is this decision that we are called upon to review. This Court has jurisdiction under 7482 Internal Revenue Code of 1954, 26 U. S. C. A. 7482.

The facts were stipulated and, unlike many tax cases, are not complicated.

During 1951 through 1955, petitioner, the largest single owner of the capital stock of Shu-Stiles, Inc., owned 3703 shares of the total of 11841 shares issued and outstanding. The remaining shares were owned by three brothers of petitioner and one person not a relative. During this same period petitioner was employed as president of the corporation and was in charge of its business and affairs.

By a 4-count indictment filed in the United States District Court for the Eastern District of Missouri on March 1, 1951, petitioner was charged with unlawfully attempting to defeat and evade a large part of the tax owed by Shu-Stiles, Inc., for the years 1942, 1943, 1944 and 1945, by filing false and fraudulent tax returns for the corporation. During those years the petitioner was president of the corporation. In due time petitioner entered a plea of guilty and was fined $10,000 on each of the counts, or a total of $40,000. Shortly after the fine was assessed, the district court, by appropriate order, directed the payment of the fine in installments over a period of approximately four years. At about the time of the conviction and the assessment of the fine, the shareholders of Shu-Stiles, Inc., in special meeting, adopted a motion which provided, in effect, that, inasmuch as the acts of petitioner, as president of the corporation, leading up to his indictment, conviction and the assessment of the fine, were done for and on behalf

of the corporation without any personal benefit from such acts, the fine should be paid by the corporation and that all expenses incurred by petitioner incidental to the indictment be assumed and paid by the corporation. Pursuant to this authorization, Sin-Stiles, Inc., paid $5,000 of the fine and $24.50 as costs in 1951, $7,500 in 1952, $10,000 in 1953, $10,000 in 1954, and $7,500 in 1955. The amounts so paid were charged against the surplus account on the books of the corporation.

Although petitioner filed personal returns for the years 1951 through 1955, he did not report as income any of the amounts paid by Sin-Stiles, Inc., in discharging his fine, and it was this failure that caused the respondent to issue notice of deficiency, determining that the amount of the fine and the court costs assumed and paid by the corporation represented "taxable income" received by petitioner in each of the respective years in which installments were paid by the corporation. From the Tax Court opinion it appears that the respondent did not originally assign any particular reason for determining that the amounts in question represented taxable income under 22(a) Internal Revenue Code, 1939, 61 Internal Revenue Code, 1954, but in the Tax Court the position was taken that the amounts paid constituted taxable dividends within the meaning of 115(a) Internal Revenue Code, 1939, and 316(a) Internal Revenue Code, 1954.

After full consideration of the applicable statutes, the decisional law, and the petitioner's contentions, the Tax Court concluded: "We think that under the authorities, which we have cited hereinabove, the payments by the corporation constituted the constructive payments of dividends to the petitioner at the times paid."

Here, as in the Tax Court, petitioner argues that the payments do not fall within the category of a dividend as-

contemplated by the statutes; that he was not benefited by the transaction and did not experience any profit or gain from the payments. He insists that we must consider the transaction in its entirety, including the factor which motivated the payment by the corporation and that when so viewed it becomes evident that the payment was made to indemnify petitioner against a loss he suffered. This is not the case.

Before attending to these contentions which go to the heart of this case, we give recognition to certain principles of law which are applicable generally when a decision of the Tax Court is under review.

In reviewing a determination of the Tax Court, the question for the Court of Appeals is whether the decision of the Tax Court is clearly wrong. **Crown Iron Works Co. v. Commissioner of Internal Rev.**, 8 Cir., 245 F. 2d 357, 358; **Lengsfield v. Commissioner of Internal Revenue**, 5 Cir., 241 F. 2d 508. This Court will not try issues of fact or substitute its judgment for that of the Tax Court respecting such issues. **Crown Iron Works Co. v. Commissioner of Internal Rev.**, supra, at p. 360; **Weiss v. Commissioner of Internal Revenue**, 8 Cir., 221 F. 2d 152, 156. And in **Boehm v. Commissioner**, 326 U. S. 287, 290, 66 S. Ct. 120, 124, 90 L. Ed. 78, the Supreme Court stated:

> "... The circumstance that the facts in a particular case may be **stipulated or undisputed** does not make this issue any less factual in nature. The Tax Court is entitled to draw whatever inferences and conclusions it deems reasonable from such facts. And an appellate court is limited, under familiar doctrines, to a consideration of whether the decision of the Tax Court is in accordance with law." 26 U. S. C. 1141 (a). If it is in accordance, it is immaterial that different inferences and conclusions might fairly be drawn from the undisputed facts. **Commissioner v.**

Scottish American Co. [illegible] (Emphasis supplied.)

Section 22 (a) of Internal Revenue Code, 1939 (as amended by Section 1, Public Salary Tax Act of 1939, c. 59, 53 Stat. 574) defines "gross income" as including "gains, profits and income derived from * * * shares * * * also from interest * * * dividends * * * or gains or profits and income derived from any source whatever * * *." Section 22 (a) provides that "Distributions by corporations shall be taxable to the shareholders as provided in section 115." Section 115 (as amended by Section 116 of the Revenue Act of 1942, c. 619, 56 Stat. 798) defines "dividend" to mean "any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year * * * without regard to the amount of the earnings and profits at the time the distribution was made. * * *." The pertinent provisions of Treasury Regulations 111, Section 29.115-1, promulgated under the Internal Revenue Code of 1939, define the term "dividend" in substantially the same language. Section 61 (a) and 316 (a) are the corresponding provisions in the Internal Revenue Code of 1954 and are substantially the same as 22 (a) and 115 (a) of the 1939 Code.

Out of the numerous cases which have been focused upon financial transactions between corporations and their shareholders, there has evolved a body of law which has given vitality to the taxing statutes under consideration. In determining the character of a corporate payment to shareholders, the courts, in looking through form to substance, have established certain criteria in determining the practical effect of such disbursements. Thus, the fact that there has been no formal declaration of dividend, or that there has been no general distribution among all share-

holders, is of no import in determining the true nature of the payment.[1] Receipts through diversion or conversion of corporate earnings and profits may be taxed as "constructive dividends."[2] Furthermore, corporate payments to third parties at the direction of shareholders, or in discharge of their personal debts and liabilities, have been ruled to be in the nature of constructive dividends, constructively received by shareholders.[3] The motive, or expressed intent of the corporation is not determinative, and constructive dividends have been found contrary to the expressed intent of the corporation.[4] The courts, as arbiters of the true nature of corporate payments, have consistently used as a standard the measure of receipt of economic benefit as the proper occasion for taxation.[5]

With the foregoing constituting a guide, it is evident that the decision of the Tax Court is not clearly erroneous. Indeed, we are convinced that the undisputed facts compel the result reached by that court. The requirements of the statute are satisfied. There was a distribution of money by Sea Strike, Inc., for the benefit of petitioner, its principal shareholder, and the distribution came out of the earnings and profits of the corporation. True, the payments were not made directly to petitioner, but legally, this circumstance is of no significance, and petitioner concedes that the payments are to be treated as though they were made to him.

The argument advanced by petitioner to the effect that the payment of the fine was in the nature of indemnity is untenable. Generally, payment made to indemnify another springs from contract, express or implied. See 42 C. J. S., Indemnity, § 2, and 27 Am. Jur., Indemnity, §§ 2 and 6. It cannot be gainsaid that an agreement to pay the penalty which might be imposed upon one found guilty of violating the law would be tainted with illegality and unenforceable. It is also settled that such a payment would not be deductible as an expense of doing business. **Tank Truck Rentals v. Commissioner**, 356 U. S. 30; **Knight-Campbell Music Co. v. Commissioner of Int. Rev.**, 10 Cir., 155 F. 2d 837. In connection with this point petitioner further urges that assessment of the fine is in the nature of a "loss" and that its payment resulted in no economic benefit. Insofar as petitioner would include a criminal fine as a category with certain recognized losses of capital such as through theft, fire and other casualties, see 165, Internal Revenue Code 1954, his contention merits no discussion. Insofar as his argument goes to a lack of economic benefit accruing to him, we need only observe that he personally was liable for payment of the fine assessed against him for his criminal act; that it was in the nature of any other private debt, and his property and assets

were liable for seizure and sale in satisfaction of the debt. See 18 U. S. C. A., 3565. We also note that under the provisions of the order of the district court, pursuant to his conviction upon indictment, petitioner was ordered imprisoned until the fine was paid, and that upon modification, providing for payments in installments, petitioner was liable to stand committed upon default of any of the installment payments. Under those facts we do not understand how petitioner can seriously argue that he received no economic benefit by reason of the corporate payment of his fines.

Petitioner relies strongly upon **Ruben v. Commissioner of Internal Revenue**, 8 Cir., 97 F. 2d 926, which involved settlement of a suit against a corporation and its shareholders. There, although the settlement and payment by the corporation in turn released the shareholder from any further claim and liability to the plaintiff in the action, the court found that no taxable benefit accrued to the shareholder, inasmuch as the corporation acted for itself and entirely in its own interest in making payment on the claim. Here the corporation was in no way involved in the criminal prosecution of petitioner. In the absence of any liability of the corporation as found in **Ruben v. Commissioner of Internal Revenue**, supra, and **Ingalls v. Patterson**, D. C. Ala., 158 F. Supp. 627, it must be held that the voluntary payment of petitioner's fine by the corporation was in effect a payment of dividends, taxable as such. Cf. **Knight-Campbell Music Co. v. Commissioner of Int. Rev.**, 10 Cir., 155 F. 2d 837, 840.

The judgment is affirmed.

A true copy.

Attest:

Clerk, U. S. Court of Appeals, Eighth Circuit.

(Judgment.)

United States Court of Appeals
for the Eighth Circuit.

No. 16353.

September Term, 1959.

Irving Sachs,
Petitioner,

vs.

Commissioner of Internal Revenue.

On Petition to Review Decision of The Tax Court of the United States.

This cause came on to be heard on the Petition to Review the Decision of The Tax Court of the United States entered July 13th, 1959, determining that that there are deficiencies in the income taxes of the Petitioner for the years 1951 through 1955, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of The Tax Court in this cause be, and the same is hereby, affirmed.

And it is further Ordered by this Court that the Petition to Review in this cause be, and the same is hereby, dismissed.

April 20, 1960.

Internal Revenue Code—1939.

Sec. 22. Gross Income—Definition. (a) General Definition. "Gross income" includes gains, profits and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid,

or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities; or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

Internal Revenue Code—1939.

115. Distributions by corporations.

(a) Definition of dividend. The term "dividend" when used in this chapter * * * means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made. * * *

Internal Revenue Code—1954.

61. Gross Income Defined.

(a) General definition.—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

(1) Compensation for services, including fees, commissions, and similar items;

(2) Gross income derived from business;

* * * * * * *

(7) Dividends;

* * * * * * *

Internal Revenue Code—1954.

316. Dividend defined.

(a) General rule.—For purposes of this subtitle, the term "dividend" means any distribution of property made by a corporation to its shareholders—

(1) out of its earnings and profits accumulated after February 28, 1913, or

(2) out of its earnings and profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year) without regard to the amount of the earnings and profits at the time the distribution was made. * * *

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FILED
AUG 11
JAMES R. BROWNING, Clerk

No. 243

In the Supreme Court of the United States

OCTOBER TERM, 1960

IRVING SACHS, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioner, the president and one-third stockholder of a corporation, was convicted of filing fraudulent tax returns for the corporation and was fined $10,000. The corporation, upon the resolution of its stockholders, paid the fine. The Tax Court and the court of appeals (Pet. 7-11[1]) held that the corporation's payment of the fine resulted in taxable income to petitioner in the nature of a dividend. That decision is clearly correct. The fine was a personal liability imposed upon petitioner for his own culpable conduct. The corporation's payment discharged petitioner's

[1] The opinion as printed in the petition does not reflect a change made by the court after its original release. The change, though seemingly unimportant, is noted in the Appendix *infra*.

legal obligation and was thus constructively received by him. Realized gains not expressely excluded by statute are within the definition of income (*Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426), and on the facts here the payments were properly characterized as dividends. There is no conflict or other reason for further review. The petition should be denied.

Respectfully submitted.

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AUGUST 1960.

APPENDIX

United States Court of Appeals
For the Eighth Circuit

[In the final opinion of the court of appeals (277 F. 2d 879, 881-882), the following paragraph was substituted for the ninth paragraph of the opinion as printed in the petition (*i.e.*, the paragraph at Pet. 10-11 beginning "In reviewing * * *"):]

* * * * * *

We are required to review the decision of the Tax Court, "in the same manner and to the same extent" as decisions of the District Courts in civil actions tried before the Judge and without a jury. § 7482, Title 26, U.S.C.A. (I.R.C. 1954). Rule 52(a), Federal Rules of Civil Procedure, 28 U.S.C.A., provides that findings of fact by the trial court shall not be set aside "unless clearly erroneous." If the Tax Court's finding here is supported by substantial evidence upon the record as a whole, and is not against the clear weight of the evidence or induced by an erroneous view of the law, it cannot be disturbed upon appeal. "A finding is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." *United States* v. *United States Gypsum Co.*, 333 U.S. 364, 395, 68 S. Ct. 525, 542, 92 L. Ed. 746, rehearing denied 333 U.S. 869, 68 S. Ct. 788, 92 L. Ed. 1147. See also *Krueger* v. *Commissioner of Internal Revenue*, 8 Cir., 269 F. 2d 184, 185, 186; *Marcella* v. *Commissioner of Internal Revenue*, 8 Cir., 222 F. 2d 878, 879; *Klamath*

Medical Service Bureau v. *Commissioner of Internal Revenue*, 9 Cir., 261 F. 2d 842, 847, certiorari denied 359 U.S. 966, 79 S. Ct. 877, 3 L. Ed. 2d 834, and compare *Crown Iron Works Co.* v. *Commissioner of Internal Revenue*, 8 Cir., 245 F. 2d 357, 358; *Longstaff* v. *Commissioner of Internal Revenue*, 5 Cir., 241 F. 2d 308.

In *Boehm* v. *Commissioner of Internal Revenue*, 326 U.S. 287, 290, 66 S. Ct. 120, 124, 90 L. Ed. 78, the Supreme Court stated:

> "* * * The circumstance that the facts in a particular case may be *stipulated or undisputed* does not make this issue any less factual in nature. The Tax Court is entitled to draw whatever inferences and conclusions it deems reasonable from such facts." Emphasis supplied.